Financial Markets

Irving Trust

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After last week's brief pause, credit markets swung back to the upside; the April rally seems to be forging ahead into May. Rates dropped sharply across the board, with the long end of the market particularly firm as heavy new supply was absorbed amid steady price gains. Optimism stemmed from a powerful combination of factors. More grim economic news led many observers to deepen recession forecasts; money and credit aggregates continued their sharp unexpected drops; and retail demand swelled as institutions stepped up buying. The only potential fly in the ointment--and the big unknown at present--is the attitude of the Federal Reserve. This week, Fed funds swung between 13% and 17%, excluding Wednesday. No one really knows how to interpret this, an uncertainty that leaves some market participants rather wary.

In the government market, announcement of next week's $7.5 billion refunding (a bit more than expected) was well received; many investors are thought to have been waiting for the announcement before buying. Rates fell in all maturities, with the bill market getting a special boost from almost $2.5 billion in Fed purchases for foreigners this week. Short-term money markets were also buoyant, and C.D. rates fell even faster than bills. More big banks cut their prime lending rates; most are now at 18.5%.

In the corporate bond markets, the flood of new issues continued, and continued to be very well received. The rush reflects pent-up borrowing needs and attractive current rates, plus the desire to get out of the way of next week's refunding. The week's corporate calendar of about $1.5 billion (close to a record) was easily absorbed--prices on average rose 3.5 points, and some supply shortage appeared late in the week. Municipals also performed well. The Bond Buyer Index fell to 7.96% from 8.11% as retail demand appeared in volume, and the recent divergence between shorter maturities (strong) and longer maturities (weak) was fading rapidly.

Economic data over the past month have signaled recession; now, the data may be signaling a worse recession than originally expected. This week saw more grim reports: auto output down again, March leading indicators down 2.6%, and March construction spending down 5.8%. The negative series was capped with Friday's report of 7.0% April unemployment, up from 6.2% in March and much higher than expected. All of this means recession, and as recessionary expectations get worse, inflationary expectations get better. Not too much weight should be given to this week's report of a 4.5% April drop in farm prices, but a major revision of inflationary expectations does seem to be contributing to the current rally.

As noted above, the enigma now is Fed policy, as revealed (or not revealed) through variations in the Fed funds rate. Since last October's switch in policy targets, the funds rate has been an unreliable policy guide, but it is still watched as the best available current indicator. Uncertainty stems from the fact that swings in funds could stem from supply (Fed policy, measured by Fed willingness to provide liquidity) or from demand for credit. Since the market does not know at present what combination of supply and demand factors produces a given movement in funds, the level of uncertainty on Fed policy--and policy prospects--is uncomfortably high.

Anne Parker Mills

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Market Yields

	5/2/80	Week Ago	Year Ago
Prime Lending Rate at Irving Trust Company	(noon)		
Short-term loans to substantial depositors with highest credit rating	18.50%	19.50%	11.75%
Effective since	5/1/80		
Discount Rate at Federal Reserve Bank	13.00/16.00	13.00/16.00	9.50
Federal Funds	14.50	15.88	10.22
Repurchase Agreements	11.75	14.50	9.00
U.S. Treasury Issues			
Bills			
3 months	10.65	12.50	10.02
6 months	10.92	12.60	10.27
1 year	10.75	11.55	10.30
Coupons			
2 years	10.56	11.50	9.91
4 years	10.62	11.34	9.36
7 years	10.56	11.11	9.34
10 years	10.52	11.03	9.37
Long Bond	10.69	11.22	9.29
Negotiable Certificates of Deposit-Secondary Market			
1 month	12.55	14.65	10.00
3 months	12.55	14.40	10.35
6 months	12.45	14.25	10.70
1 year	11.60	N/A	10.80
Banker's Acceptances			
1 month	12.32	14.30	9.98
3 months	12.42	14.35	10.30
6 months	12.50	14.25	10.64
Eurodollar Deposits			
1 month	14.00	16.13	10.56
2 months	14.13	16.31	10.81
3 months	14.13	16.38	10.88
Commercial Paper - Prime Names			
Directly placed by:			
Finance Companies			
1 week	11.00	10.00	9.50
1 month	11.25	12.00	9.75
3 months	10.75	12.00	9.63
Bank Holding Companies			
1 month	12.00	13.75	9.75
Dealer Placed:			
3 months	12.00	12.00	9.88
New AA Corporate Utility Bond	13.70	14.50	10.20
Tax Exempt			
6 month Project Notes	6.25	6.75	5.20
1 year AAA Bond	6.05	6.40	N/A
5 year AAA Bond	6.10	6.50	N/A
20 year AAA Bond	7.30	7.50	5.85

This information represents prevailing market yields.

It should not be construed as an offering.

All yields are on the offered side of the market.

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